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THE TAX LAWYER

TAXES 11/30/2016

Court Allows IRS John Doe Summons For Bitcoin, Other Virtual Currencies

A federal court in the Northern District of California has [entered an order authorizing the IRS to serve a John Doe summons on Coinbase Inc.](#) The IRS goal is information about U.S. taxpayers who conducted transactions in a convertible virtual currency during 2013 to 2015. The IRS is seeking the records of Americans who engaged in business with or through, a virtual currency exchanger headquartered in San Francisco.

“As the use of virtual currencies has grown exponentially, some have raised questions about tax compliance,” said Principal Deputy Assistant Attorney General Caroline D. Ciralo, head of the Justice Department’s Tax Division. “Tools like the John Doe summons authorized today send the clear message to U.S. taxpayers that whatever form of currency they use – bitcoin or traditional dollars and cents – we will work to ensure that they are fully reporting their income and paying their fair share of taxes.”

“Transactions in virtual currency are taxable just like those in any other property,” said IRS Commissioner John Koskinen. “The John Doe summons is a step designed to help the IRS ensure people doing business in the emerging economy are following the tax laws and meeting their responsibilities.”



(Photographer: Chris Ratcliffe/Bloomberg)

Virtual currency, as generally defined, is a digital representation of value that functions in the same manner as a country's traditional currency. There are nearly a thousand virtual currencies, but the most widely known and largest is bitcoin. Because transactions in virtual currencies can be difficult to trace and have an inherently pseudo-anonymous aspect, taxpayers may be using them to hide taxable income from the IRS. In the [court's order](#), U.S. Magistrate Judge Jacqueline Scott Corley found that there is a reasonable basis for believing that virtual currency users may have failed to comply with federal tax laws.

The IRS has issued guidance regarding the tax consequences on the use of virtual currencies in [IRS Notice 2014-21](#), which provides that virtual currencies that can be converted into traditional currency are property for tax purposes, and a taxpayer can have a gain or loss on the sale or exchange of a virtual currency, depending on the taxpayer's cost to purchase the virtual currency (that is, the taxpayer's tax basis).

The court's order grants the IRS permission to serve a "John Doe" summons on Coinbase. There is no allegation in this suit that Coinbase has engaged in any wrongdoing in connection with its virtual currency exchange business. Rather, the IRS uses John Doe summonses to obtain information about possible violations of internal revenue laws by *others*, individuals whose identities are unknown. This John Doe summons directs Coinbase to produce records identifying U.S. taxpayers who have used its services, along with

other documents relating to their virtual currency transactions.

With a normal summons, the IRS seeks information about a *specific* taxpayer whose identity it knows. In contrast, a John Doe summons allows the IRS to get the names of *all taxpayers* in a certain group. A John Doe summons is ideal for pursuing account holders at a financial institution. After sniffing out American taxpayers with UBS accounts, the IRS did the same with HSBC in India and [Citibank and BofA in Belize](#). The IRS uses John Doe summonses when it doesn't know the identities of the suspected culprits. And while it will take the IRS time to collate and process it, you can bet the IRS will put the information it acquires to good use.

For alerts to future tax articles, email me at Wood@WoodLLP.com. This discussion is not legal advice.